

[DISCUSSION DRAFT]108TH CONGRESS
1ST SESSION**H. R.** __________
IN THE HOUSE OF REPRESENTATIVESM____. _____ introduced the following bill; which was referred to the
Committee on _____
_____**A BILL**

To improve transparency relating to the fees and costs that
mutual fund investors incur and to improve corporate
governance of mutual funds.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Mutual Funds Integ-
5 rity and Fee Transparency Act of 2003”.



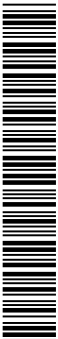
1 **SEC. 2. IMPROVED TRANSPARENCY OF MUTUAL FUND**
2 **COSTS.**

3 (a) REGULATION REVISION REQUIRED.—Within 270
4 days after the date of enactment of this Act, the Securities
5 and Exchange Commission shall revise regulations under
6 the Securities Act of 1933, the Securities Exchange Act
7 of 1934, or the Investment Company Act of 1940, or any
8 combination thereof, to require, consistent with the protec-
9 tion of investors and the public interest, improved disclo-
10 sure with respect to an open-end management investment
11 company, in the quarterly statement or other periodic re-
12 port to shareholders or other appropriate disclosure docu-
13 ment, of the following:

14 (1) The estimated amount, in dollars, of the op-
15 erating expenses of the company that are borne by
16 each shareholder.

17 (2) The structure of, or method used to deter-
18 mine, the compensation of individuals employed by
19 the investment adviser of the company to manage
20 the portfolio of the company.

21 (3) The portfolio transaction costs of the com-
22 pany, including commissions paid with respect to the
23 trading of portfolio securities, set forth in a manner
24 that facilitates comparison among investment com-
25 panies.



1 (4) Information concerning the company's poli-
2 cies and practices with respect to the payment of
3 commissions for effecting securities transactions to a
4 member of an exchange, broker, or dealer who—

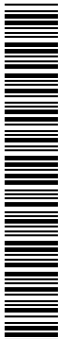
5 (A) furnishes advice, either directly or
6 through publications or writings, as to the value
7 of securities, the advisability of investing in,
8 purchasing, or selling securities, and the avail-
9 ability of securities or purchasers or sellers of
10 securities;

11 (B) furnishes analyses and reports con-
12 cerning issuers, industries, securities, economic
13 factors and trends, portfolio strategy, and the
14 performance of accounts; or

15 (C) facilitates the sale and distribution of
16 the company's shares.

17 (5) Information concerning payments by any
18 person other than the company that are intended to
19 facilitate the sale and distribution of the company's
20 shares.

21 (6) Information concerning discounts on front-
22 end sales loads for which investors may be eligible,
23 including the minimum purchase amounts required
24 for such discounts.



1 (b) DEFINITION.—For purposes of subsection (a), a
2 disclosure shall not be considered to be made in an appro-
3 priate disclosure document if the disclosure is made exclu-
4 sively in a prospectus or statement of additional informa-
5 tion, or both such documents.

6 **SEC. 3. OBLIGATIONS REGARDING CERTAIN DISTRIBUTION**
7 **AND SOFT DOLLAR ARRANGEMENTS.**

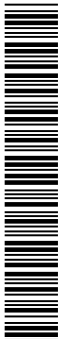
8 Section 15 of the Investment Company of 1940 (15
9 U.S.C. 80a-15) is amended by adding at the end the fol-
10 lowing new subsection:

11 “(g) OBLIGATIONS REGARDING CERTAIN DISTRIBUTION AND SOFT DOLLAR ARRANGEMENTS.—

12 “(1) REPORTING REQUIREMENTS.—Each in-
13 vestment adviser to a registered investment company
14 shall, no less frequently than annually, submit to the
15 board of directors of the company a report on—

16 “(A) payments during the reporting period
17 by the adviser (or an affiliated person of the
18 adviser) that were directly or indirectly made
19 for the purpose of promoting the sale of shares
20 of the investment company (referred to in para-
21 graph (2) as a ‘revenue sharing arrangement’);

22 “(B) services to the company provided or
23 paid for by a broker or dealer or an affiliated
24 person of the broker or dealer (other than bro-
25



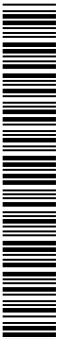
1 kerage and research services) in exchange for
2 the direction of brokerage to the broker or deal-
3 er (referred to in paragraph (2) as a ‘directed
4 brokerage arrangement’); and

5 “(C) research services obtained by the ad-
6 viser (or an affiliated person of the adviser)
7 during the reporting period from a broker or
8 dealer the receipt of which may reasonably be
9 attributed to securities transactions effected on
10 behalf of the company or any other company
11 that is a member of the same group of invest-
12 ment companies (referred to in paragraph (2)
13 as a ‘soft dollar arrangement’).

14 “(2) FIDUCIARY DUTY OF BOARD OF DIREC-
15 TORS.—The board of directors of a registered invest-
16 ment company shall have a fiduciary duty—

17 “(A) to supervise the investment adviser’s
18 direction of the company’s brokerage trans-
19 actions, including directed brokerage arrange-
20 ments and soft dollar arrangements, and to de-
21 termine that the direction of such brokerage is
22 in the best interests of the shareholders of the
23 company; and

24 “(B) to supervise any revenue sharing ar-
25 rangements to ensure compliance with this Act



1 and the rules adopted thereunder, and to deter-
2 mine that such revenue sharing arrangements
3 are in the best interests of the shareholders of
4 the company.

5 “(3) REGULATIONS.—The Commission shall
6 adopt rules and regulations implementing this sec-
7 tion, which rules and regulations shall, among other
8 things, prescribe the content of the required reports.

9 “(4) DEFINITION.—For purposes of this
10 subsection—

11 “(A) the term ‘brokerage and research
12 services’ has the same meaning as in section
13 28(e)(3) of the Securities Exchange Act of
14 1934; and

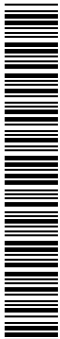
15 “(B) the term ‘research services’ means
16 the services described in subparagraphs (A) and
17 (B) of such section.”.

18 **SEC. 4. MUTUAL FUND GOVERNANCE.**

19 (a) DIRECTOR AND CHAIRMAN INDEPENDENCE.—
20 Section 10(a) of the Investment Company Act of 1940 (15
21 U.S.C. 80a–10) is amended—

22 (1) by striking “60 per centum” and inserting
23 “one-third”; and

24 (2) by inserting “, nor shall such registered
25 company have as chairman of such board an inter-



1 ested person of such registered company” before the
2 period.

3 (b) DEFINITION OF INTERESTED PERSON.—Section
4 2(a)(19) of the Investment Company Act of 1940 (15
5 U.S.C. 80a-2(a)(19)) is amended—

6 (1) in subparagraph (A)—

7 (A) by striking clause (vi) and redesignig-
8 nating clause (vii) as clause (vi); and

9 (B) by amending clause (v) to read as fol-
10 lows:

11 “(v) any natural person who is a
12 member of a class of persons who the
13 Commission, by rule or regulation, deter-
14 mines are unlikely to exercise an appro-
15 priate degree of independence as a result
16 of—

17 “(I) a material business or pro-
18 fessional relationship with the com-
19 pany or any affiliated person of the
20 company, or

21 “(II) a close familial relationship
22 with any natural person who is an af-
23 filiated person of the company,”; and

24 (2) in subparagraph (B)—



1 (A) by striking clause (vi) and redesignig-
2 nating clause (vii) as clause (vi); and

3 (B) by amending clause (v) to read as fol-
4 lows:

5 “(v) any natural person who is a
6 member of a class of persons who the
7 Commission, by rule or regulation, deter-
8 mines are unlikely to exercise an appro-
9 priate degree of independence as a result
10 of—

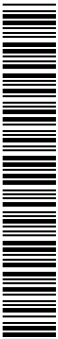
11 “(I) a material business or pro-
12 fessional relationship with such invest-
13 ment adviser or principal underwriter
14 (or affiliated person thereof), or

15 “(II) a close familial relationship
16 with a natural person who is such in-
17 vestment adviser or principal under-
18 writer (or affiliated person thereof).”.

19 **SEC. 5. AUDIT COMMITTEE REQUIREMENTS FOR INVEST-**
20 **MENT COMPANIES.**

21 (a) AMENDMENTS.—Section 32 of the Investment
22 Company Act of 1940 (15 U.S.C. 80a-31) is amended—

23 (1) by striking paragraphs (1) and (2) of sub-
24 section (a) and inserting the following:



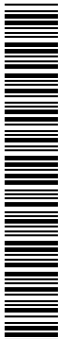
1 “(1) such accountant shall have been selected
2 at a meeting held within 30 days before or after the
3 beginning of the fiscal year or before the annual
4 meeting of stockholders in that year by the vote,
5 cast in person, of a majority of the members of the
6 audit committee of such registered company;

7 “(2) such selection shall have been submitted
8 for ratification or rejection at the next succeeding
9 annual meeting of stockholders if such meeting be
10 held, except that any vacancy occurring between an-
11 nual meetings, due to the death or resignation of the
12 accountant, may be filled by the vote of a majority
13 of the members of the audit committee of such reg-
14 istered company, cast in person at a meeting called
15 for the purpose of voting on such action;” and

16 (2) by adding at the end the following new sub-
17 section:

18 “(d) AUDIT COMMITTEE REQUIREMENTS.—

19 “(1) REQUIREMENTS AS PREREQUISITE TO FIL-
20 ING FINANCIAL STATEMENTS.—Any registered man-
21 agement company or registered face-amount certifi-
22 cate company that files with the Commission any fi-
23 nancial statement signed or certified by an inde-
24 pendent public accountant shall comply with the re-
25 quirements of paragraphs (2) through (6) of this



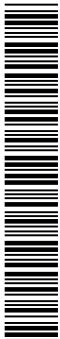
1 subsection and any rule or regulation of the Com-
2 mission issued thereunder.

3 “(2) RESPONSIBILITY RELATING TO INDE-
4 PENDENT PUBLIC ACCOUNTANTS.—The audit com-
5 mittee of the registered company, in its capacity as
6 a committee of the board of directors, shall be di-
7 rectly responsible for the appointment, compensa-
8 tion, and oversight of the work of any independent
9 public accountant employed by such registered com-
10 pany (including resolution of disagreements between
11 management and the auditor regarding financial re-
12 porting) for the purpose of preparing or issuing the
13 audit report or related work, and each such inde-
14 pendent public accountant shall report directly to
15 the audit committee.

16 “(3) INDEPENDENCE.—

17 “(A) IN GENERAL.—Each member of the
18 audit committee of the registered company shall
19 be a member of the board of directors of the
20 company, and shall otherwise be independent.

21 “(B) CRITERIA.—In order to be considered
22 to be independent for purposes of this para-
23 graph, a member of an audit committee of a
24 registered company may not, other than in his
25 or her capacity as a member of the audit com-



1 mittee, the board of directors, or any other
2 board committee—

3 “(i) accept any consulting, advisory,
4 or other compensatory fee from the reg-
5 istered company or any affiliated person of
6 the registered company; or

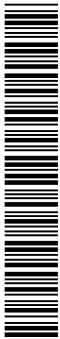
7 “(ii) be an ‘interested person’ of the
8 registered company, as such term is de-
9 fined in section 2(a)(19).

10 “(4) COMPLAINTS.—The audit committee of the
11 registered company shall establish procedures for—

12 “(A) the receipt, retention, and treatment
13 of complaints received by the registered com-
14 pany regarding accounting, internal accounting
15 controls, or auditing matters; and

16 “(B) the confidential, anonymous submis-
17 sion by employees of the registered company
18 and its affiliated persons of concerns regarding
19 questionable accounting or auditing matters.

20 “(5) AUTHORITY TO ENGAGE ADVISERS.—The
21 audit committee of the registered company shall
22 have the authority to engage independent counsel
23 and other advisers, as it determines necessary to
24 carry out its duties.



1 “(6) FUNDING.—The registered company shall
2 provide appropriate funding, as determined by the
3 audit committee, in its capacity as a committee of
4 the board of directors, for payment of
5 compensation—

6 “(A) to the independent public accountant
7 employed by the registered company for the
8 purpose of rendering or issuing the audit re-
9 port; and

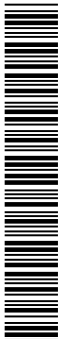
10 “(B) to any advisers employed by the audit
11 committee under paragraph (5).

12 “(7) AUDIT COMMITTEE.—For purposes of this
13 subsection, the term ‘audit committee’ means—

14 “(A) a committee (or equivalent body) es-
15 tablished by and amongst the board of directors
16 of a registered investment company for the pur-
17 pose of overseeing the accounting and financial
18 reporting processes of the company and audits
19 of the financial statements of the company; and

20 “(B) if no such committee exists with re-
21 spect to a registered investment company, the
22 entire board of directors of the company.”.

23 (b) CONFORMING AMENDMENT.—Section 10A(m) of
24 the Securities Exchange Act of 1934 is amended by add-
25 ing at the end the following new paragraph:



1 “(7) EXEMPTION FOR INVESTMENT COMPA-
2 NIES.—Effective one year after the date of enact-
3 ment of the Mutual Funds Integrity and Fee Trans-
4 parency Act of 2003, for purposes of this subsection,
5 the term ‘issuer’ shall not include any investment
6 company that is registered under section 8 of the In-
7 vestment Company Act of 1940.”.

8 (c) IMPLEMENTATION.—Not later than 180 days
9 after the date of enactment of this Act, the Securities and
10 Exchange Commission shall issue final regulations to
11 carry out section 32(d) of the Investment Company Act
12 of 1940, as added by subsection (a) of this section.

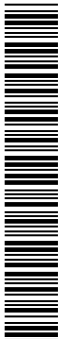
13 **SEC. 6. COMMISSION STUDY AND REPORT REGULATING**
14 **SOFT DOLLAR ARRANGEMENTS.**

15 (a) STUDY REQUIRED.—

16 (1) IN GENERAL.—The Commission shall con-
17 duct a study of the use of soft dollar arrangements
18 by investment advisers as contemplated by section
19 28(e) of the Securities Exchange Act of 1934 (15
20 U.S.C. 78bb(e)).

21 (2) AREAS OF CONSIDERATION.—The study re-
22 quired by this section shall examine—

23 (A) the trends in the average amounts of
24 soft dollar commissions paid by investment ad-



1 visers and investment companies in the past 3
2 years;

3 (B) the types of services provided through
4 soft dollar arrangements;

5 (C) the extent to which use of soft dollar
6 arrangements impairs the ability of mutual
7 fund investors to evaluate and compare the ex-
8 penses of different mutual funds;

9 (D) the conflicts of interest created by soft
10 dollar arrangements;

11 (E) the transparency of such soft dollar
12 arrangements to investment company share-
13 holders and investment advisory clients of in-
14 vestment advisers; and

15 (F) whether such section 28(e) should be
16 repealed or modified.

17 (b) REPORT REQUIRED.—The Commission shall sub-
18 mit a report on the study required by subsection (a) to
19 the Committee on Financial Services of the House of Rep-
20 resentatives and the Committee on Banking, Housing and
21 Urban Affairs of the Senate, no later than 18 months
22 after the date of enactment of this Act.

